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No. 374

In the Supreme Court of the United States

OCTOBER TERM, 1932

THE PEOPLE OF THE STATE OF NEW YORK,
PETITIONERS

v.

MARK M. MACLAY AND CHARLES E. MCWILLIAMS, RECEIVERS OF MCWILLIAMS BROS., INC., AND UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

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OPINIONS BELOW

The opinion of the District Court (R. 18) is not reported. The opinion of the Circuit Court of Appeals (R. 22–28) is reported in 59 F. (2d) 979.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 20, 1932. (R. 28.) The petition for certiorari was filed September 17, 1932, and was granted October 24, 1932. (R. 29.) Jurisdic-

tion is conferred upon this Court by Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether Section 3466 of the Revised Statutes gives priority to the United States for tax and other claims against an insolvent debtor over claims of the State of New York for franchise and gross earnings taxes due from the debtor, in view of a declaration in the New York statutes to the effect that such taxes are to be liens against the property of the taxpayer.

STATUTES INVOLVED

The applicable provisions of the statutes involved are set forth in the Appendix (*infra*, pp. 13–16).

STATEMENT

The receivers of the insolvent[1] McWilliams Bros., Inc., requested the District Court for the

[1] For convenience, throughout this brief, McWilliams Bros., Inc., is referred to as the "insolvent." Receivers were appointed upon the filing of a creditor's bill alleging that the corporation's assets exceeded its liabilities and praying for the appointment of a receiver, and an answer admitting the allegations of the bill and joining in the prayer for relief. (R. 23.) Under these circumstances the receivership amounted to a voluntary assignment (*Price* v. *United States*, 269 U. S. 492, 502), and the right of the United States to priority was therefore the same as if the corporation had been insolvent. (R. 23.) Furthermore, it is obvious that the corporation was in fact insolvent or it would have been unnecessary to have an order determining priorities.

Southern District of New York to determine the amounts and validity of certain claims of the United States and of the State of New York against the insolvent, and the respective priorities, if any, of these claims. (R. 6–9.) The attorneys for the United States and the State of New York stipulated the facts applicable to this determination, of which the following is a summary (R. 9–12):

Temporary receivers, appointed January 10, 1927, by court order, were made permanent January 29, 1927. (R. 10.) About March 24, 1927, the United States filed a claim for $516.46 with the receivers for expenses incurred in replacing one of its buoys which was run into by a tug of the insolvent and lost. Previously, on January 25, 1927, the United States had filed a claim for additional income tax against the insolvent for a period in 1917, in the amount of $5,263.24. This assessment was made March 8, 1923. The United States also filed a similar claim for income taxes for 1918 in the amount of $28,400.73. This assessment was made September 15, 1925. (R. 10–11.)

The State of New York, about September 16, 1927, entered a claim of $2,317.82 for franchise and gross earnings taxes due it for the years 1921 to 1925, inclusive, under Sections 182 and 184 of the Tax Law of that State. On January 12, 1928, the State of New York gave notice of a similar claim in regard to taxes against the insolvent for 1925, 1926, 1927, and subsequent years. On January 5,

1929, the State sent the receivers a liquidated claim for these taxes in the amount of $813.23, some of these taxes being for the period after the appointment of the receivers. (R. 7–8, 12.)

Both the United States and the State of New York agree that the claims of each party are valid in the amounts stated and that the only question is with respect to the right to priority of payment of these claims. (R. 12.)

The District Court held a hearing on the matter of priority of these claims (R. 12–18) and subsequently determined that the claims of the United States should be paid before those of the State of New York (R. 18–19). The Circuit Court of Appeals affirmed this order. (R. 28.)

SUMMARY OF ARGUMENT

This Court held in *Spokane County* v. *United States,* 279 U. S. 80, that the claims of the United States prevailed over those of a State by virtue of Section 3466 of the Revised Statutes, although the State statutes granted a general lien for taxes upon all the property of the taxpayers which, in the particular case, had not been perfected as a lien upon specific property. In the instant case, Section 201 of the New York Tax Law did provide a method whereby a specific lien could be created to cover unpaid taxes. This section has not been complied with. In view of the provisions of Section 201, Section 197 of that law, as construed by the courts, must be considered as creating only a gen-

eral lien, in the nature of an extension of the common law right of the sovereign to priority of payment of its debts, which when it conflicts with that of the United States, as in this case, must give precedence to the latter.

ARGUMENT

In the instant case the sole question is whether the provisions of the New York Tax Law create a lien, on account of taxes due the State of New York from an insolvent, which will take precedence over tax and other claims of the United States which otherwise would be given priority of payment by Section 3466 of the Revised Statutes (*infra*, p. 13) out of the insolvent's estate.

The question whether claims of the United States rather than those of a State should be paid first out of an insolvent's estate has been considered by this Court recently in *Spokane County* v. *United States*, 279 U. S. 80. In that case it was held that the lien given by a statute of the State of Washington, as construed by the State courts, was of such a general character that it did not supersede the priority of the United States if at the time this priority attached there had not been a distraint by the sheriff or any other procedure essential to make the lien specific.

The interpretation of the statute by the State court was that the general statutory declaration of a lien created merely an inchoate tax lien right against the property of the taxpayer which was not

perfected as a specific lien until the prescribed procedure was completed with reference to the particular property involved. In view of the decision in the *Spokane case,* the court below appears to have correctly narrowed the precise problem now involved when it stated (R. 26)—

> While it is clear that in the present case the taxes due the state of New York prior to the receivership were a general lien upon the real and personal property of the defendant at the time when the receivers were appointed, the question is not whether these taxes are statutory liens of some sort, but whether they are such liens as the courts of the United States have recognized as entitled to priority over claims due the government.

The priority of the United States, if any, attached, under Section 3466 of the Revised Statutes, when the receiver was appointed. *United States* v. *Oklahoma,* 261 U. S. 253, 260. This priority applied to taxes due as well as to other debts. *Price* v. *United States,* 269 U. S. 492, 499. It is settled by the decisions of this Court that a mortgage of real estate is a conveyance of such an interest as will defeat the priority given by the above section. *Savings Society* v. *Multnomah County,* 169 U. S., 421, 428; *Brent* v. *Bank of Washington,* 10 Pet. 596; *Conard* v. *Atlantic Insurance Co.,* 1 Pet. 386. But it has been held that the United States will take priority over the lien of a judgment creditor who

has not levied an execution against the debtor's property. *Thelusson* v. *Smith,* 2 Wheat. 396. The authority of the United States, in exercising its taxing power, to secure priority in payment of its claims over those of the States, is clear, and Section 3466 is to be liberally construed to achieve this end. *Spokane County* v. *United States, supra,* at p. 93. Whenever the powers of the United States and those of a State conflict, the latter must yield, even though this interferes with the exercise of its full powers of taxation. *Florida* v. *Mellon,* 273 U. S. 12, 17.

When the receivers in the present suit were appointed, the United States had assessed the income taxes against the insolvent which are the basis of the Government's tax claims involved in the present suit, and the insolvent at that time was liable for damages to property of the United States. The insolvent also was indebted to the State of New York for franchise taxes for 1921 and subsequent years, which were imposed by Section 182 of the Tax Law of that State. Later, the claims for franchise taxes were extended to include those for the years up to and including 1929. The State also had claims for gross earnings taxes against the insolvent for the same period (excepting 1929) imposed under Section 184 of the Tax Law. Section 197 of the New York Tax Law (*infra,* p. 14) provided that the taxes imposed by Sections 182 and 184, among others, should be a lien upon the per-

sonal and real property of the taxpayer until the taxes were paid in full. Previously, this section had contained a provision to the effect that the lien for such a tax should apply "from the time when it is payable."

In *N. Y. Terminal Co.* v. *Gaus,* 204 N. Y. 512, it was held that this section, at the time that it contained this proviso, created a lien on property from the time the tax became payable, which took priority over the interest of a mortgagee. See also *Engelhardt* v. *Alvino Realty Co.,* 248 N. Y. 374. Section 197 and the *N. Y. Terminal Co. case* were considered by this Court in *Marshall* v. *New York,* 254 U. S. 380. It was there pointed out (pp. 382–384) that this section was an extension of the common law right inherent in the State of New York as a soverign, whereby it had priority over other creditors for the payment of its claims. At common law, it was said, this right did not prevail over a specific lien created by the debtor before the sovereign exercised its right to payment, but the New York legislature had extended this right so as to give certain taxes priority in payment over previous incumbrances. The omission of the phrase, "from the time when it is payable," from Section 197 as in effect when the taxes in question became due, has been held not to have changed the time when the liens for such taxes arose, and this is still the time when the taxes are payable. The lien attaches at that time, notwithstanding that the

amount of the tax has not been computed. *Carey* v. *Keith, Inc.*, 250 N. Y. 216.

The distinction between general and specific liens, which was the basis of the decision in the *Spokane case,* does not appear to have been considered by the New York courts in relation to the statutes of that State involved in the present case. However, it has been held that an agreement between private parties to the effect that one should have a "lien" on the property of the other created only a general lien and not a specific one. *Rohrbach* v. *Germania Fire Ins. Co.*, 62 N. Y. 47, 52. It may, therefore, be argued that since Section 197 provides merely that a "lien" is created on the taxpayer's property, the decision in the *Rohrbach case* indicates that the statute, in employing the same word used in the agreement there considered, does not create a specific lien, but only a general lien.

Another strong indication that Section 197 did not create a specific lien, within the meaning of the *Spokane case,* is that Section 201 of the New York Tax Law (*infra,* p. 14) provides that if the amount stated in a tax account is not paid within thirty days from the sending of a notice of such an account, the tax commission may issue a warrant directed to the proper sheriff commanding him to levy upon and sell the real and personal property of the taxpayer for the payment of taxes. This section provides, among other things, that:

> Such warrant shall be a lien upon and shall bind the real and personal property * * *

> from the time an actual levy shall be made by virtue thereof.

The section also provides that the sheriff shall proceed in the same manner under such a warrant as is done in respect to executions issued against property upon judgments of courts of record. There is nothing in the record in the instant case to indicate that any action had been taken under this section. Its provisions indicate that the lien given by Section 197 is similar to that of the judgment creditor considered in *Thelusson* v. *Smith, supra,* which did not become specific until an execution had been levied against particular property. The preference given to the State over mortgagees of the debtor by Section 197, as this Court stated in *Marshall* v. *New York, supra,* must be taken to be no more than an extension of the common law priority of the sovereign in payment of its debts in preference to certain incumbrances.

From the above analysis of the New York statutes it is apparent that in the instant case the court below correctly held that the State of New York did not acquire such a definite interest in the insolvent's property by virtue of Section 197 as to distinguish the State's claim for priority in the payment of taxes from the claim of the State considered in the *Spokane decision, supra.* Accordingly we believe that the decision in that case controls this one.

The situation resolves itself into a conflict between the respective priorities of the United States

and those of the State of New York, in which case the claims of the United States must prevail. *Spokane County* v. *United States, supra.* What was said by this Court in *Lane County* v. *Oregon,* 7 Wall. 71, is particularly pertinent here. There the statement was made that (p. 77):

> * * * In respect, however, to property, business, and persons, within their (the United States and the States) respective limits, their power of taxation remained and remains entire. It is indeed a concurrent power, and in the case of a tax on the same subject by both governments, *the claim of the United States, as the Supreme authority, must be preferred;* but with this qualification it is absolute. * * * (Italics ours.)

See also the statement of this Court in *United States* v. *Snyder,* 149 U. S. 210, at page 214. In *United States* v. *Oklahoma, supra,* it was said at page 260 that "* * * The priority given the United States [by Section 3466 of the Revised Statutes] can not be impaired or superseded by state law. * * *" See also *Bramwell* v. *U. S. Fidelity Co.,* 269 U. S. 483; *United States* v. *Butterworth Corp.,* 269 U. S. 504; *Merryweather* v. *United States,* 12 F. (2d) 407 (C. C. A. 9th); *In re Essenkay Products Co.* 5 F. (2d) 668 (C. C. A. 7th); *Central Trust Co.* v. *Third Av. R. Co.,* 186 Fed. 291 (C. C. A. 2nd); *Stover* v. *Scotch Hills Coal Co.,* 4 F. (2d) 748 (W. D. Pa.); and *United States* v. *San Juan County,* 280 Fed. 120 (W. D. Wash.).

Contra, In re A. E. Fountain, Inc., 295 Fed. 873 (S. D. N. Y.).

CONCLUSION

The judgment of the Circuit Court of Appeals was correct and should be affirmed.

Respectfully submitted.

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APPENDIX

Revised Statutes:

SEC. 3466. Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority hereby established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed. (U. S. C., Title 31, Sec. 191.)

SEC. 3184. Where it is not otherwise provided, the collector shall in person or by deputy, within ten days after receiving any list of taxes from the Commissioner of Internal Revenue, give notice to each person liable to pay any taxes stated therein, to be left at his dwelling or usual place of business, or to be sent by mail, stating the amount of such taxes and demanding payment thereof. If such person does not pay the taxes, within ten days after the service or the sending by mail of such notice, it shall be the duty of the collector or his deputy to collect the said taxes with a penalty of five per centum additional upon the amount

of taxes, and interest at the rate of one per centum a month. (U. S. C., Title 26, Sec. 104.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 875:

SEC. 613. LIEN FOR TAXES.—(a) Section 3186 of the Revised Statutes, as amended, is amended to read as follows:

"SEC. 3186. (a) If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person. Unless another date is specifically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time.

"(b) Such lien shall not be valid as against any mortgagee, purchaser, or judgment creditor until notice thereof has been filed by the collector * * *." (U. S. C. Sup., Title 26, Sec. 115.)

New York Tax Law, Consol. Laws, c. 61, provides in part as follows:

SEC. 197. * * * Each such tax or fee [including those imposed by Sections 182 and 184 of the New York Tax Law] shall be a lien and binding upon the real and personal property of the corporation * * * liable to pay the same until the same is paid in full. * * *

SEC. 201. *Warrant for the collection of taxes.*—After the expiration of thirty days from the sending by the commission of a

notice of a statement of an account as provided in this article, unless the amount of such account shall have been paid or deposited with the tax commission, if an appeal or other proceedings have been taken to review the same, and the undertaking given as provided in this article, the tax commission may issue a warrant under its official seal, directed to the sheriff of any county of the state, commanding him to levy upon and sell the real and personal property of the persons, partnerships, company, association, or corporation against which such account is stated, found within his county for the payment of the amount thereof with interest thereon and costs of executing the warrant, and to return such warrant to the tax commission and pay to the tax commission the money collected by virtue thereof, by a time to be therein specified, and not less than sixty days from the date of the warrant. Such warrant shall be a lien upon and shall bind the real and personal property of the person, partnership, company, association, or corporation against which it is issued, from the time an actual levy shall be made by virtue thereof. The sheriff to whom any such warrant shall be directed shall proceed upon the same in all respects, with like effect, and in the same manner as prescribed by law in respect to executions issued against property upon judgments of a court of record, and shall be entitled to the same fees for his services in executing the warrant, to be collected in the same manner. In case any warrant pursuant hereto is returned unsatisfied, or is not returned satisfied within thirty days after the date when such warrant is made returnable, the tax commission may

proceed upon the warrant in all respects, with like effect, and may deputize any assistant, or other officer or other employee of the tax department to so execute the warrant, and shall be entitled to the same fees for services as the sheriff is entitled to charge.

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